



Vermont Department of Labor
Updated and Abbreviated
Proposal 10/28/09

Unemployment Insurance Reform Proposal

Introduction:

This is an updated Unemployment Insurance Trust Fund proposal from the Vermont Department of Labor for the Legislative Study Committee. This is an abbreviated proposal for the committee members. We have removed the background information on how the trust fund got to this position and other comparison data in the previous proposal. The Study Committee has received this information in separate documents and presentations. The full proposal is on our web site for public review.

This update changes the proposal submitted starting in January 2009 and updated in April, 2009. This updated proposal reflects the following factors:

- Ø October 2009 updated consensus unemployment rate projections from Tom Kavet and Jeff Carr. The model lists the actual projected rates.
- Ø The increase in taxable wage base to \$10,000 effective January 1, 2010, as approved by the Legislature during the special session in June 2009.
- Ø The freeze on maximum weekly benefits at the current \$425 as approved by the Legislature during the special session in June 2009.
- Ø Increased projected borrowing of \$110 million by the end of 2010. This is an increase of \$30 million dollars over projected borrowing in the April proposal. This increase is due primarily to insufficient action in 2009 with respect to taxable wage base increases and benefit restrictions.

Outcomes of this proposal.

- Û This proposal projects the trust fund will return to a positive balance by 2015.
- Û The fund balance will be over \$200 million by 2018 and on the way to solvency.
- Û The tax increases are phased in over a four year period.
- Û Interest payments are limited to 5 years. Maximum borrowing of approximately \$170 million.
- Û FUTA tax increases are limited to 4 years.
- Û Addresses the seasonal worker and negative balance employers.
- Û Benefits adjustments still provide some of the more generous in the country.
- Û Indexing helps assure the fund remains solvent.

The Need for Reform

Vermont's unemployment insurance system needs reform. After years with a healthy trust fund, the system is soon to have a negative balance. To remain fiscally viable, the system needs some combination of more revenue and adjustments to benefit payments. Vermont workers have received more in benefits than employers have paid in taxes during 14 of the last 20 years.

The current economic downturn is exacerbating the problem. Higher unemployment will increase payments but the revenue stream will reach its maximum potential by 2010. The trust fund model projections show benefits increasing to \$110 million in 2010 with an assumption of 8.1% average unemployment. Contributions will total approximately \$68 million in 2010 due in part to the increase in the taxable wage base enacted by the Legislature. Higher unemployment speeds the decline of the trust fund. The system cannot continue in its present form without severe consequences to Vermont and its economic base.

What Are the Consequences of not Reforming UI?

1. Vermont will have to take cash advances from the federal unemployment trust fund of more than \$344 million even after using all available federal stimulus funds to pay benefits over the next few years.
2. States may take cash advances from Federal unemployment trust funds. However, if the funds are not repaid by the end of September during the following year, interest will accrue. Currently the interest rate is 4.64 percent.
3. Interest payments cannot come from unemployment taxes so this will be a general fund obligation.
4. The current Federal tax rate is 0.8% of the first \$7000 in wages. If advances are not repaid by September 30 of the year in which borrowed, employers lose 0.3 percentage points of their federal tax credit, effectively increasing the federal tax by 50% the year after a balance remains. Each year the tax credit will decline until the balance is repaid or employers are paying the full FUTA tax of 6.2%.
5. While Federal law has a provision to request a freeze on FUTA tax credit losses, Vermont will not be eligible to request such a freeze until 2015 due to the relationship between effective tax rate and benefit costs. ***This updated proposal will result in no borrowing by 2015.***
6. Repaying cash advances through the loss of tax credits effectively shifts relative costs to all employers rather than to those whose employees get benefits. There is no experience rating in federal unemployment tax law.

7. Projections show Vermont will need to take cash advances indefinitely once the fund is emptied, unless reforms are enacted.
8. Under current Vermont law, when Vermont takes cash advances to pay unemployment benefits, the maximum benefit amount is frozen.

What is the Solution?

An equitable solution must include both benefit and revenue changes. This is especially true to avoid long term borrowing.

I) Contribution adjustments:

1) Increase Employer Contributions to the Trust Fund: Phase in taxable wage base (TWB) increases over four years starting in calendar year 2010. The Legislature has already increased the TWB from \$8,000 to \$10,000 effective January 1, 2010. We are recommending continued phased in increases to the TWB as follows:

From \$10,000 to \$12,000 in 2011
From \$12,000 to \$15,000 in 2012.
From \$15,000 to \$18,000 in 2013.

The already enacted Legislative change will increase contributions by \$14 million in 2010. The additional increases will generate \$28 million in 2011, \$22 million in 2012 and \$20 million in 2013 assuming employment does not decline beyond current forecast. This is a total of \$84 million over a four year period.

This proposal indexes taxable wage base to the growth in the average wage when the contribution rate returns to schedule III of the tax tables. We also propose adding a statutory trigger to reduce TWB tied to the health of the fund. Currently, as the fund grows, tax schedules are adjusted downward. However, to avoid the fund growing beyond amounts needed to sustain solvency through future recessions, our proposal includes a mandatory trigger to reduce TWB to \$16,000 when the contribution rate returns to schedule I of the tax tables or when the fund balance exceeds \$325,000,000 as of April 1st following the last calendar year of experience.

2) Do not relieve an employer from charges to their experience rating when that employer is non-responsive to initial requests for information from the Department and if that

employer fails to participate in subsequent fact finding or appeals. Presently, if benefits have been awarded to a claimant because information provided indicated eligibility and we later find out from the employer that benefits should not have been awarded, we must relieve the employer's experience rating from any charges associated with the claim. This results in charges to the trust fund, but not to the employer's experience rating. Typically, the information supporting denial of benefits is provided by the employer well after the initial inquiry from the Department. This would place the burden on the employer to return initial requests timely and participate in all applicable appeals. As it is today, there is no financial burden for a non-responding/non-participating employer.

3) Charge a fee to reimbursable employers. Presently, reimbursable employers are billed for benefits paid to their workers. The benefits are effectively borrowed from the trust fund costing the system money through lost interest when the fund has a positive balance or increased interest when the fund is insolvent. We propose adding a 1% fee to all charges to reimbursable employers that would be deposited into the trust fund to help ameliorate the cost to tax paying employers. This would cost public and non-profit employers an estimated \$64,000 a year.

II) Benefit adjustments:

1) Reduce the maximum weekly benefit from \$425 to \$400. Nationally the base maximum weekly benefit ranges from a low of \$235 in MS to a high of \$628 in MA. In New England the base maximum weekly benefits range from \$628 in Massachusetts to \$344 in Maine. This change would keep Vermont with the 24th highest maximum weekly benefit of all states. This proposal would also include freezing the automatic increase in the maximum weekly benefit amount until tax schedule III is reached. The lower maximum weekly benefit will help address the increased projected borrowing. **This reduction will save approximately \$5 million in 2010.**

In addition, the maximum weekly benefit must be capped at \$400 for the duration of borrowing. Failure to cap will result in decreasing efforts to return the fund to solvency in a reasonable period of time and would contribute to increased loss of FUTA credits.

2) Modify the weekly benefit amount to be based on four quarters of earnings and not the current two. Currently the weekly benefit amount (WBA) is calculated by dividing the total of the 2 highest quarters of wages in the base period by 45. This results in every WBA being based on just 2 quarters of employment. This means that someone working 2 quarters a year in theory would receive the same WBA as someone who worked all four quarters if the same wages were made in each quarter worked. Our new proposal calculates the WBA taking into consideration employment throughout the entire base period by calculating the average of all four quarters and dividing the average by 23 to get the same 57% of wage replacement that exists today. This also addresses the concern for certain seasonal workers that can work 6 months and collect unemployment for six months. This approach is a more accurate reflection of wages earned and ties unemployment insurance to wages earned.

3) Limit eligibility to workers with a significant attachment to the labor market by eliminating one of the three methods to determine a weekly benefit amount. The majority of claimants are found eligible for a weekly benefit amount using the first method, which is all wages paid during the first four of the last five completed quarters. (If a benefit year were established today, we would use wages paid during quarters ending 2/08 through 1/09.) We propose eliminating the 3rd method, which was used in 3% of claims filed in FY 08. Vermont is one of only two states that has 3 methods to find an individual monetarily eligible for UI benefits, whereas 16 (Maine, New York, and New Hampshire included) other states use the two methods. **Items 2 & 3 will save approximately \$11.5 million annually.**

4) A person fired for misconduct is disqualified from receiving benefits until they earn 4 times their weekly benefit amount. Presently if someone is fired for misconduct, defined as “substantial disregard of an employer’s interest,” they can still collect unemployment benefits for the full 26 weeks after a 9 week delay. Many employers believe an employee should be disqualified from receiving benefits for misconduct. This change will result in the worker needing to earn wages and become unemployed through no fault of their own, which is the current laws of most states, as well as all border states. **This reduction will save \$2.9 million annually.**

5) Prohibit workers fired for gross misconduct from using the wages paid by that employer to qualify for benefits. Currently workers separated for serious (gross) misconduct (such as theft or violence at the workplace) must return to work and earn wages 6 times their weekly benefit amount. This change proposes an additional consequence for serious misconduct by eliminating the use of such wages from computation of the weekly benefit amount.

6) Reduce earnings disregard from 30% to 20%. Presently, if a person is working part-time, they can earn up to 30% of their weekly benefit amount and see no reduction in benefits. This would reduce that to 20% of their weekly benefit amount. Example: An individual with a weekly benefit amount of \$425 earning \$300 would receive \$252 in UI; with this change, the UI payment would reduce to \$210. **This change will save \$877,000 annually.**

7) Re-institute the one week waiting period for benefits that was eliminated in 2000. This would require laid off workers to wait one week before filing for benefits. We are one of only 13 states with no waiting period. Data suggests unemployed workers seek new work faster if there is a waiting period. Further, a majority of employers pay in arrears. Meaning most workers receive their last paycheck during that first week of filing. **This change will save \$8.3 million in 2010 but less in subsequent years.**

8) Order repayment of benefits by claimants when those benefits have been erroneously awarded. Presently, with few exceptions, the only time we recoup previously paid benefits is if the erroneous payment resulted from misrepresentation by the claimant. This

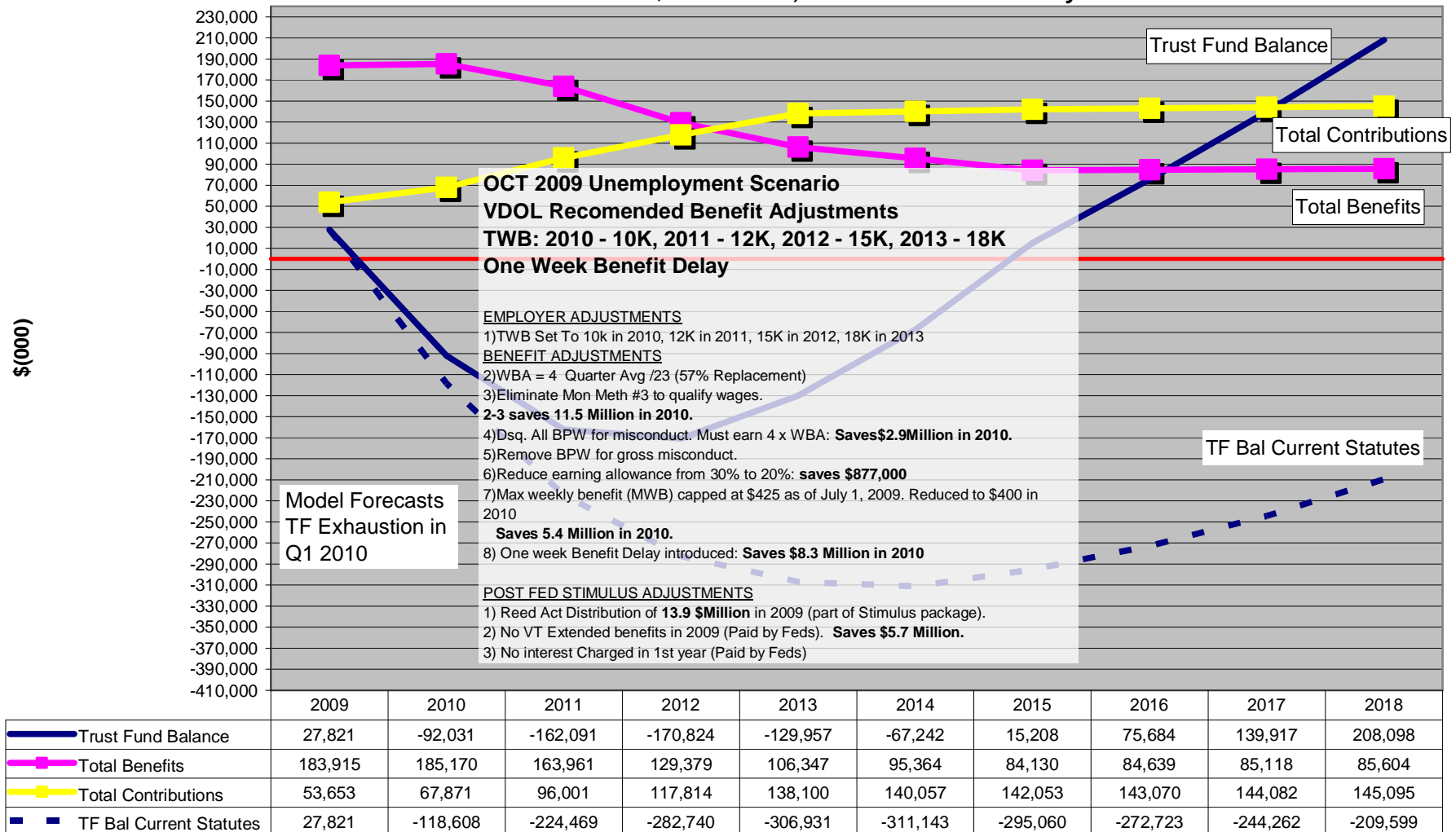
provision would require a claimant to repay those benefits regardless. It would also result in the trust fund being reimbursed for benefits improperly paid. This is tied to #2 above in that we are essentially “requiring” employers to participate timely in requests for information.

9) Remove the option enabling claimants to collect UI while receiving severance pay.

Presently employers may opt to allow their laid off employees to receive benefits during a period they are receiving severance pay; essentially double-dipping. Disqualifying severance pay, the same as wages in lieu of notice and vacation pay are handled, will ultimately result in the claimants having a longer duration of income (allocated severance pay followed by unemployment benefits) should subsequent employment not be found. Further, employers who are closing or moving out of state will not be paying future increased taxes which puts further strain on the fund.

10/16/2009

**Vermont UI Trust Fund Projection: Oct 2009 Unemployment Scenario -
VDOL Rec Benefit Adj. TWB = 10K in 2010, 12K in 2011, 15K in 2012 and 18K in 2013,
MWB Reduced to \$400 in 2010, One Week Benefit Delay**



SOURCE: VDOL Benefit Finance Model, October, 2009

Oct Forecast Scenario: VDOL Recommended Benefit Adj. TWB+ 10K - 12K 15K - 18K, 1 week delay 10/16/09

	Interest	Trust Fund	Regular	Extended	Total	Total	Taxable	Total
Year	Earned (000)	Balance (000)	Benefits (000)	Benefits (000)	Benefits (000)	Contributions (000)	Wages (\$Mil.)	Wages (\$Mil.)
2009	3,866	27,821	183,915	0	183,915	53,653	1,867	8,024
2010	207	-92,031	176,216	8,955	185,170	67,871	2,243	8,124
2011	0	-162,091	160,464	3,497	163,961	96,001	2,653	8,336
2012	0	-170,824	126,456	2,923	129,379	117,814	3,257	8,608
2013	0	-129,957	106,347	0	106,347	138,100	3,818	8,932
2014	0	-67,242	95,364	0	95,364	140,057	3,874	9,237
2015	130	15,208	84,130	0	84,130	142,053	3,929	9,552
2016	1983	75,684	84,639	0	84,639	143,070	3,958	9,839
2017	5244	139,917	85,118	0	85,118	144,082	3,986	10,134
2018	8667	208,098	85,604	0	85,604	145,095	4,014	10,438

Year	TUR	Wage Growth	Labor Force Growth	Taxable Wage Base	Max Weekly Benefit	Tax Rate Schedule
2008	4.90	3%	0%	8,000	409	4
2009	7.20	2%	0%	8,000	425	4
2010	8.10	2%	0%	10,000	400	5
2011	7.40	2%	0%	12,000	400	5
2012	5.90	3%	0%	15,000	400	5
2013	5.00	3%	0%	18,000	400	5
2014	4.50	3%	0%	18,000	400	5
2015	4.00	3%	0%	18,000	400	5
2016	4.00	3%	0%	18,000	400	5
2017	4.00	3%	0%	18,000	400	5
2018	4.00	3%	0%	18,000	400	5

Year	Interest Rate %	Cash Advance Amt (Mil.)	Interest Payable September 30 (Mil.)	FUTA Credit Reduction %	FUTA Credit Reduction Payment Jan 1 (Mil.)	Avg Cost of FUTA Credit Reduction per Ins. Emp.	Avg. Cost per Ins Emp (except FUTA)
2009	4.62	0.0	0.0	0	0.0	0.0	255.85
2010	4.62	92.0	0.0	0	0.0	0.0	326.10
2011	4.78	162.1	6.1	0.3	0.0	0.0	458.58
2012	4.7	170.8	8.1	0.6	5.9	27.9	555.88
2013	4.68	130.0	7.4	0.9	11.9	55.9	646.79
2014	4.63	67.2	4.9	1.2	18.2	84.9	653.31
2015	4.73	0.0	2.4	0	24.5	114.0	659.96
2016	4.91	0.0	0.0	0	0.0	0.0	664.69
2017	5	0.0	0.0	0	0.0	0.0	669.39
2018	5.06	0.0	0.0	0	0.0	0.0	674.10
TOTALS		170.8	28.8		60.6		